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DEPARTMENT PLEASE PASS TO NSC FOR ADAM STERLING

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SUBJECT: BETTER THAN (CONSERVATIVELY) EXPECTED: FINANCE
MINISTER VERES ON REVENUE AND REFORM

Classified By: P/E COUNSELOR ERIC V. GAUDIOSI; REASONS 1.4 (B) AND (D)

¶1. (C) A relaxed and upbeat Finance Minister Veres told Ambassador Foley April 4 that deficit reduction efforts are exceeding the GoH's conservative projections, with the GoH lowering the 2006 budget deficit to 9.2% of GDP rather than the anticipated 10.1%. He noted that the GoH was cautiously - and quietly - optimistic that 2007 figures would also be better than forecast based on figures from the first quarter.

¶2. (C) Responding to Ambassador Foley's question regarding his confidence in the Ministry's forecasting, Veres laughingly admitted to a very "prudent" philosophy in the Ministry's projections. However, he also cited improved revenue collection efforts and stricter government spending as contributing factors. He believes the positive trend will continue in 2007 as the government reduces its spending, suggesting that GDP growth will exceed the projected rate of 2.2%.

¶3. (C) Veres also sees minimal impact from the referenda proposed by the opposition to challenge elements of the government's reform agenda. Noting the law's prohibition on referenda addressing budgetary issues, he believes only the referenda on land sales, pharmaceuticals, and citizenship for ethnic Hungarians will survive legal review. He also predicted that the referendum would fail to receive the requisite 50% turn-out required by law "if tuition and doctor's fees" are not included."

¶4. (C) Turning to the contentious issue of replacing Hungary's "expected tax," Veres rolled his eyes and noted that the current debate did not reflect his understanding with Minister of Economy (and now SZDSZ party president) Koka last year. He believes the recent Court ruling overturning the expected tax will cost the GoH HF 30 billion in revenue this year, but observed that improved tax collection and existing budgetary reserves should cover the shortfall. By 2008, he plans to have stricter corporate auditing measures in place to recoup the revenue through improved collection. Corporations reporting no profits will be the target of increased tax audit efforts.

¶5. (C) Regarding the question of property tax, Veres acknowledged Ambassador Foley's observation that the GoH would do well to "get all the bad news over with in 1 year." He noted consensus within the coalition regarding tax reform, and predicted a government decision to move forward on the real estate tax - and to eliminate other existing taxes - this month. He indicated that the object of the move would be to provide a uniform system of assessing value, but noted that the primary object of the exercise would be to broaden the tax base, not to assess market value.

¶6. (C) Veres closed with a brief aside regarding criticism

from the World Bank and IMF, suggesting that they are "never satisfied." That said, he expressed his personal pride in the GoH's commitment to doing the right - and unpopular - thing. He believes the government's current efforts are at "the edge of feasibility," and knows the public will judge them based on their results.

FOLEY